Primer on IFRS 17

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IFRS 17 Primer

Section 1 - Introduction, Scope and Purpose

In May 2017, the International Accounting Standards Board (IASB) issued the final draft International Financial Reporting Standard 17 *Insurance Contracts* (IFRS 17 or "the Standard") to establish "principles for the recognition, measurement, presentation, and disclosure of insurance contracts." Since IFRS 17 will be effective January 1, 2023, the Casualty Actuarial Society's Committee on Reserves has prepared this primer for members who may be less familiar with the Standard's issues and challenges.

IFRS 17 will supersede IFRS 4, which has been in effect as a placeholder for IFRS 17 since January 1, 2005. A principal shortcoming of IFRS 4 is that it permits the use of various accounting practices, which may vary by jurisdiction (for example, IFRS 4 permits the use of US GAAP, where applicable). In other words, IFRS 4 maintains the status quo and allows the use of prevailing accounting standards in place by jurisdiction. As a result, it is difficult for interested parties to fully understand, compare and combine the financial results of insurers and reinsurers across various jurisdictions. The purpose of IFRS 17 is to implement one accounting standard across the world and to create consistency in accounting practices for insurance contracts.

For Property/Casualty insurance entities, IFRS 17 is applicable to insurance and reinsurance contracts they issue and purchase.

The focus of this IFRS 17 primer is specific to property and casualty insurance contracts. The primer describes key components of IFRS 17 on a broad basis and compares the new standard to current accounting standards in place in the US (GAAP and/or Statutory Accounting Principles). It does not provide an exhaustive reference to all the changes that IFRS 17 will require.

- Section 1 addresses the background related to IFRS 17 and introduces nomenclature and basic terminology;
- Section 2 discusses the concept of insurance contracts in detail;
- Section 3 addresses the recognition and measurement of insurance contracts;
- Section 4 addresses financial statement disclosures related to insurance contracts.

Nomenclature & Terminology

The following terms and their definitions will be useful as you read through the remainder of the paper:

- *Insurance Contract*

  A contract under which one party (the issuer) accepts significant **insurance risk** from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder.

- *Liability for Remaining Coverage ("LRC")*

  This term corresponds to **Unearned Premium Reserve or UPR.**

- *Liability for Incurred Claims ("LIC")*

  This term corresponds to **Unpaid Loss and Loss Adjustment Expense Reserves.**

- *Portfolio of Contracts*

  A portfolio of contracts consists of policies that are subject to similar risks and managed together.

- *Risk Adjustment for Non-financial risk ("RA")*

  Compensation an entity requires for bearing the uncertainty about the amount and timing of the cash flows that arises from insurance (or non-financial) risk as the entity fulfils insurance contracts.

  This term corresponds to **Risk Margin.**

- *Financial Risk*

  Risk associated with changes in financial variables such as interest rates and underlying asset values. Generally, financial variables are broad based measures of financial performance and are not specific to a party participating in the insurance contract.

- *Compensation*

  Compensation is the amount the insurer provides to the insured to settle its obligations under the contract. Compensation is not required to be monetary; certain contracts may allow or require claims to settle in kind (e.g., replacement of stolen object, medical services provided by policyholders that are health care providers).

- *Fulfilment Cash Flows ("FCFs")*

  The FCFs are the sum of three key components:

  1. Best estimate cash flows (probability-weighted expected cash flows over **all potential** outcomes);
  2. Adjustment for the time value of money;
  3. Risk adjustment for insurance (or non-financial) risk.

  The use of FCFs to measure insurance contracts is comparable to the concept of fair value under US GAAP, used for purchase accounting. Purchase GAAP (P-GAAP) reflects discount for the time value of money and an explicit risk margin. These two FCF components represent a significant change for most US actuaries.

  In measuring insurance contracts, FCFs are the basis for the calculations of the Liability for Remaining Coverage ("LRC") and the Liability for Incurred Claims ("LIC").

- *Onerous Contracts*

  If a contract's initial FCF are a negative outflow at initial recognition, then the contract is deemed to be onerous (unprofitable).

- *Insurance Acquisition Cash Flows*

  IFRS 4 permits a company to hold an asset for pre-paid acquisition costs directly related to insurance contracts as deferred acquisition costs (DAC). Under IFRS 17, the acquisition cash flows directly attributable to a group of contracts are an asset until the recognition of its related insurance contracts. After the initial recognition, acquisition cash flows are incorporated in the LRC. Hence pre-paid acquisition costs are recognized as offsets to future payments in the determination of the LRC. Acquisition costs that are not directly attributable to insurance contracts to which the group of contracts belong are not incorporated in the LRC and are recognized as paid.

- *Generalized Measurement Model (GMM)*

  The Standard describes how to measure insurance contract liabilities. Initially, this is the LRC, which then gives rise to LIC. The process followed to do this is the Generalized Measurement Model and it is based on the Fulfilment Cash Flows (FCFs).

- *Contractual Service Margin (CSM)*

  The CSM represents an entity's estimate of the profit it expects to earn as it provides insurance services to its policyholders included in a portfolio of contracts.

- *Premium Allocation Approach (PAA)*

  An entity can apply a simplification to the GMM called the Premium Allocation Approach (PAA) to particular groups of contracts. For this approach, "premium" can be allocated over the coverage period. The PAA provides a comparable liability to the UPR in the US statutory framework. The PAA is discussed in more detail below.

Section 2 - Insurance Contracts

Scope

The contracts within the scope of IFRS 17 are:

- Insurance contracts (including reinsurance contracts) an entity issues
- Ceded reinsurance contracts an entity holds
- Investment contracts with discretionary participation features an entity issues, provided that the entity issues insurance contracts

The third item generally applies to life insurance contracts, so it will not be covered in this document.

An insurance contract is defined as a contract in which one party (the issuer) accepts **significant insurance risk** from another party (the policyholder) by agreeing to compensate the policyholder if a specified **uncertain future event (the insured event**) adversely affects the policyholder.

The definition of an insurance contract includes the term "significant insurance risk." This is defined in Appendix A of IFRS 17 as "risk, other than financial risk, transferred from the holder of the contract to the issuer."

An insurance contract is in scope of IFRS 17 if it transfers a significant amount of insurance risk to the primary insurer or reinsurer.

- Insurance risk is present if a covered event can cause the insurer to pay out significant amounts under any scenario, irrespective of the likelihood of such a scenario. *This is a significant difference compared to current US GAAP and SAP, which require significant probability and significant amount of loss to demonstrate risk transfer.*
- Even if a reinsurance contract does not expose the issuer to the possibility of a significant loss, the contract is deemed to transfer significant insurance risk if it transfers to the reinsurer substantially all the insurance risk relating to the reinsured portions of the underlying insurance contracts.[1]

Moreover, an insured event is defined as "An uncertain future event covered by an insurance contract that creates insurance risk." In Appendix B of the Standard, Paragraphs B3 to B5 provide guidance on what an uncertain future event refers to when applying this definition:

[1] IFRS 17 §B19

- The uncertainty can relate to one or more of the probability, timing or size of the event. *It includes the case where the event has already occurred, but the amount and timing are uncertain.*
- The insurance risk must have an adverse effect on the policyholder and is transferred to the insurer by the insurance contract.[2]
- This adverse effect of the uncertain event on the policyholder is a necessary contractual precondition for a contract to meet the definition of an insurance contract.[3]

Components

Boundary of the Contract

Paragraph 34 of the standard defines the boundary of a contract for IFRS 17 measurement purposes.

"Cash flows under IFRS 17 are within the boundary of a contract if they arise from substantive rights and obligations that exist during the reporting period in which the entity can compel the policyholder to pay the premiums, or in which the entity has a substantive obligation to provide the policyholder with services."

Thus, the contract boundary classifies future cash flows to be considered in the measurement of the contract and also determines where the contract ends for measurement purposes.

[2] IFRS 17 §B11

[3] IFRS 17 §B13

Coverage Period

The Coverage Period is defined as the period during which the entity provides coverage for insured events. This period includes the coverage that relates to all premiums within the boundary of the insurance contract.

Components accounted for under other IFRSs

Components in an insurance contract such as distinct investment components, distinct service components and, where required by IFRS 9, embedded derivatives, must be separated from the insurance contract measurement.

An example of a distinct investment component is the fund related to a universal life policy. Examples of distinct service components are claims service for large deductible policies and claims service when the entity is acting as a third-party administrator ("TPA").

IFRS 17 defines investment component as "the amounts that an **insurance contract** requires the entity to repay to a **policyholder** in all circumstances, regardless of whether an **insured event** occurs."

The Exposure Draft of the Proposed International Actuarial Note (IAN) 100 (paragraphs B31 and B32) on Application of IFRS 17 Insurance Contracts states the following:

"Investment components are to be separated if and only if they are distinct, which means that both of the following conditions are met:

- *The investment component is not highly interrelated with the insurance component; this means both that the entity is able to measure each component without considering the other components and policyholders can benefit from each component even if the other is not present (e.g., each component can lapse independently).*
- *The investment component appears after some reasonable research to be, or could be, sold separately in the same market or jurisdiction."*

Examples of <u>non-distinct</u> investment components are:

- Claims-free bonus
- Sliding scale commissions on reinsurance contracts
- Contractual profit-sharing mechanisms
- Retro-rated workers compensation policies

Contracts and their Grouping

In determining the level of aggregation, an entity must first identify portfolios of contracts. A portfolio comprises of contracts subject to similar risks and that are managed together. A group of insurance contracts is a partition of a portfolio according to when the contract is issued and its expected profitability.

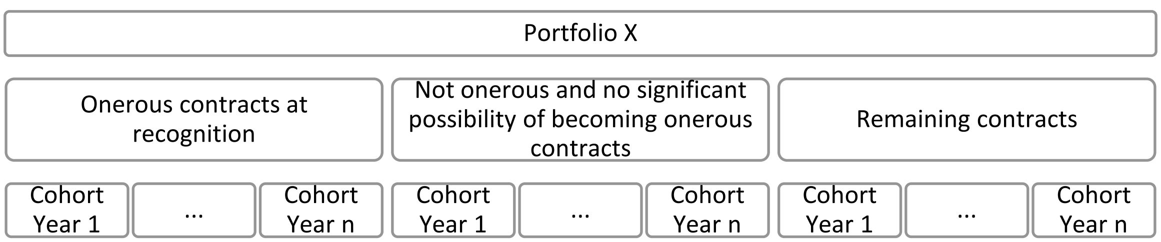
Each portfolio must be divided into a minimum of three groups:

1. Onerous contracts (unprofitable or loss-making),
2. Not Onerous and no significant possibility of becoming onerous, and
3. Remaining contracts

A contract within a portfolio is required to be assigned one of the three groups at the initial recognition of a contract, divided into groups that are one year or less apart. It is expected that most contracts are expected to be assigned to Group 3.

The level of aggregation determines the recognition and measurement requirements of IFRS 17.[4]

The figure below illustrates the concepts of this section for a given portfolio:



Cohort refers to a group of contracts or policies. It is expected that the determination of portfolios may vary across entities, and also may be different within a given entity as it changes the way it manages its business over time.

A contract is recognized at the earlier of the date when insurance coverage commences or the date the initial premium becomes due. A contract might be recognized earlier if it turns out to be onerous.[5] It should be noted that if the LIC and LRC amounts are calculated at a higher level of aggregation, an allocation at a group level will be required.

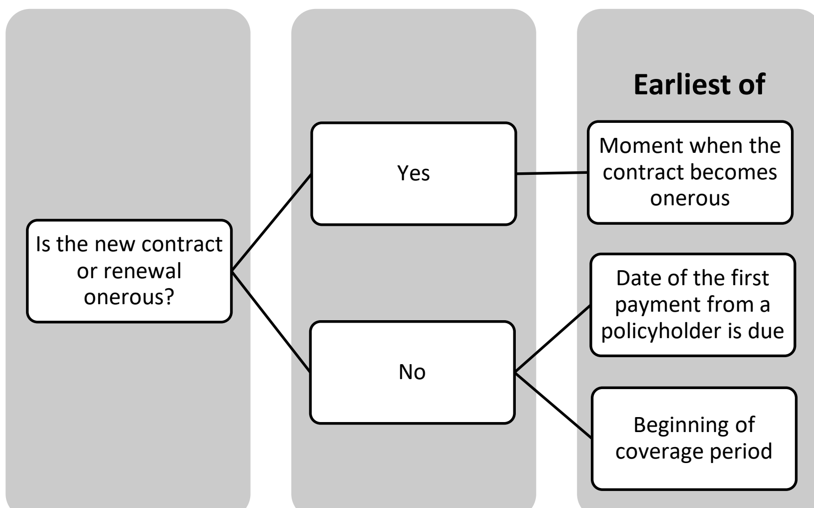
[4] IFRS 17 §24

[5] IFRS 17 §25

Section 3 - Recognition

Initial recognition and subsequent measurements of liabilities

The starting point in measurement of an entity's liabilities is the recognition of a group of contracts. Recall that the group belongs to a portfolio of contracts that are "subject to similar risks and managed together"[6]. For a group of contracts, it will be first recognized (and thus reported) at the earliest of the: 1) date at which coverage begins; 2) date at which the first payment from a policyholder is due (receipt of policyholder's payment is equivalent to the due date[7]); and 3) date at which the group becomes onerous.[8] For example, based on an updated actuarial study, it becomes evident that a current and a renewal assumed reinsurance contract is unprofitable (onerous), the renewal contract would need to be recognized immediately. The figure below illustrates this concept:



As the recognition date is the earliest of these, it is incumbent on the entity to determine if a group is onerous prior to the effective date or when premium is due if facts and circumstances so indicate.[9] This does not preclude that a contract can be issued prior to recognition. Any cash flows related to insurance acquisition expenses related to those issued contracts need to be considered as well. Once a contract has been assigned to a group, it remains in that group until it is derecognized,[10] which can

[6] IFRS 17 §14

[7] IFRS 17 §26

[8] IFRS 17 §25

[9] IFRS 17 §26

[10] IFRS 17 §24

occur only under certain modifications of the original contract or by the extinguishment of all liabilities of the contract.[11] Generally, modifications for non-life contracts are rare.

It should be noted that renewal notices are usually sent a few months in advance. For onerous contracts or groups of contracts, renewals agreed a few months in advance will need to be included in the calculation of LRC.

Fulfilment Cash Flows

A key component in determining insurance assets or liabilities under IFRS 17 is the determination of fulfilment cash flows (FCF). There are three components of the FCF[12]:

1) Estimates of future cash flows. These include both inflows (premiums) and outflows (payments for claims, acquisition and administration expenses). These are the probability weighted mean over the full range of the possible outcomes[13];
2) Adjustments to reflect the time value of money in relation to the financial risks associated with those future cash flows to the extent that financial risk is not included within those future cash flows; and
3) Risk adjustment for non-financial risk (i.e. the risk margin). As the estimates for the liabilities are to be current, the FCF will need to be updated at each evaluation in the life of an insurance contract.

At initial recognition and when updating the measurement for a group of contracts, the entity will consider all of the cash flows within the boundary for each of the underlying contracts. Cash flows are within the boundary of an insurance contract if they "arise from substantive rights and obligations that exist during the reporting period in which the entity can compel the policyholder to pay the premiums or in which the entity has a substantive obligation to provide the policyholder with services"[14].

This obligation ends when either:

1) The entity can re-evaluate the risks of a particular policyholder and is able to set a new premium (but there is no obligation to do so) or;

2) The entity is able to revalue the risks in a portfolio that includes the contact while updating the premium or benefit level as well as the original premium not being determined with risks relating to the period after this date of re-evaluation.

[11] IFRS 17 §§72, 74

[12] IFRS 17 §32

[13] IFRS 17 §33(a)

[14] IFRS 17 §34

Frequently, the Standard states that exercises such as this should use information available without undue cost or effort. In this case, the Standard anticipates that the entity would have already put forth most of the effort required in the deriving liabilities for other reporting purposes.

In order to incorporate the time value of money related to the expected cash flows, the appropriate discount rate should reflect the attributes of the cash flows and the liquidity features of the insurance contracts. Further, the rates need to be consistent with observable market interest rates of financial instruments having cash flow characteristics similar to the insurance contracts.[15] For cash flows that do not vary based upon the returns of the underlying items, e.g., workers compensation liabilities, the discount rate for the appropriate currency reflects the yield curve that exposes the holder to little or no credit risk when considering the liquidity characteristics of the corresponding insurance contracts.[16]

The Standard goes on to require the determination of the risk adjustment for non-financial risk. The calculation is to be explicit, disclosed and reconciled separately.[17] This margin for risk represents the compensation that an insurer requires in order to assume the risk related to the uncertainty and the timing of the expected cash flows. The adjustment should reflect the diversification of the insurance risk portfolio.[18]

At initial recognition, the Standard describes how to measure the liabilities that the entity will place on its balance sheet. This process to be followed is called the GMM (Generalized Measurement Model). When a group of contracts is first measured under the GMM, the liability for that group equals the sum of its FCF (Fulfilment Cash Flows) plus the CSM (Contractual Service Margin), provided the contract is not onerous. The CSM represents the unearned profit the entity expects to earn as it provides insurance services to its policyholders within that group of contracts.[19] This initial liability resides entirely within the LRC. Thus, at initial recognition, no income arises from the recognition of the contract and the initial cash flows exchanged at that date as well as de-recognition of all cash flows exchanged prior to initial recognition.[20]

If, however, a contract's initial FCF are a negative outflow at initial recognition, then the contract is defined as being onerous. Further, the entity is obligated to group onerous contracts separately from those contracts deemed not onerous.[21] For simplicity, an

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[15] IFRS 17 §36

[16] IFRS 17 §B79

[17] IFRS 17 §§33, 100

[18] IFRS 17 §§37, B88

[19] IFRS 17 Appendix A

[20] IFRS 17 §38

[21] IFRS 17 §47

entity may measure a set of contracts as onerous rather than individual contracts. For an onerous group, an entity will establish a Loss Component (LC) to recognize the loss within that group and the amount will be excluded from insurance revenue.[22] A contract is onerous at initial recognition if it's FCF plus any previously recognized acquisition costs plus any cash flows create a negative net outflow.[23] In this light, the Standard effectively creates an equivalent to a premium deficiency reserve on those groups of contracts that are onerous. It is possible that a group not initially onerous could become onerous. At this point, the CSM (Contractual Service Margin) will become nil. The LC (Loss Component) will then take on the value of the present value of the future loss in excess of what the LRC (Liability for Remaining Coverage) would have been with a nil CSM. It is possible for this LC to reverse subsequently and the CSM can be re-established.

Thereafter, all subsequent measurements of the liabilities will be the sum of the LRC and the LIC (Liability for Incurred Claims). The LRC will represent the FCF related to future service for the group at the evaluation date including the CSM at that date (or if the CSM is nil, a value for the LC will be determined). The LIC for the group at the evaluation date will represent the FCF related to past service allocated to that group.[24]

Under the GMM, for non-onerous contracts, the LRC equals the sum of:

- Expected value of future cash flows (both inflows and outflows)
- Adjustment for the time value of money
- RA (Risk Adjustment) for non-financial risk
- Maximum of 0 or the CSM

The CSM is calculated at initial recognition and each subsequent measurement until exhausted at the end of the coverage period for every contract in the group. For the period from time, t-1, to time, t, the value of CSM (t)[25] is equal to the sum of:

- CSM(t-1)
- CSM for contracts being added to the group of contracts since time, t-1
- Interest accreted on the carrying amount of the CSM since time, t-1
- Adjustments to the FCF relating to future service since time, t-1
- Effect of any currency exchange differences on the CSM

[22] IFRS 17 §49. Recall in IFRS 17 §16, an entity is required to divide a portfolio of contracts into a minimum of three groups of contracts: 1) a group that is onerous at initial recognition; 2) a group at initial recognition with no chance of becoming onerous; and 3) a group of remaining contracts.

[23] IFRS 17 §47

[24] IFRS 17 §40

[25] One could consider that CSM (0) to be the contractual service margin at initial recognition for a group of contracts with nil value prior.

- Reduction by the transfer of the amount recognized as insurance revenue due to the risk being moved to insurance contract services, i.e., from the LRC to LIC, since time, t-1

Note that the discount rate at which the CSM is accreted is that rate that was determined for the group of contracts at initial recognition.[26] The discount rate at initial recognition may incorporate the weighted average discount rates over the period in which the contracts within the group were issued.[27]

An entity can apply a simplification to the GMM as a "simplified approach," called the Premium Allocation Approach (PAA), to particular groups of contracts where an allocation of "premium" may be applied over the coverage period.[28] One may use the PAA for a group of contracts provided at the group's inception one of the following is applicable:

1) The entity anticipates that the result of the calculation of the LRC would not be materially different from the one derived from the GMM or;

2) The coverage period for each contract in the group is no more than one year.

Under 1) above, a group cannot use this simplification if the entity anticipated high variability in the cash flows prior to claims being incurred. [29] The PAA provides a comparable liability to the UPR that is prevalent within the US statutory and US GAAP environment.

Generally, an entity cannot use the PAA for onerous contracts.[30] However, for Property and Casualty entities, the coverage period for each contract within a group rarely exceeds one year. In this instance, the PAA can be used for a group of contracts where no single contract has a coverage period in excess of one year regardless of the onerousness of the group of contracts.[31]

The LRC under the PAA (LRC_{PAA}) is calculated at initial recognition and each subsequent measurement until exhausted. For the period from time, t-1, to time, t, the value of LRC_{PAA} (t)[32] when the group of contracts is not onerous is equal to the sum of:

- LRC_{PAA}(t-1)

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[26] IFRS 17 §B72

[27] IFRS 17 §B73

[28] IFRS 17 §IN8

[29] IFRS 17 §§53, 54

[30] IFRS 17 §18

[31] IFRS 17 §53

[32] IFRS 17 §55

- Premiums received between t-1 and t
- Reduced by insurance acquisition cash flows paid between t-1 and t (unless the entity chooses to recognize the payments as an expense)
- Amortization of insurance acquisition cash flows recognized as an expense in the reporting period
- Adjustment for financing component reflecting the time value of money, if applicable
- Reduced by the amount recognized as insurance revenue for services provided from t-1 to t

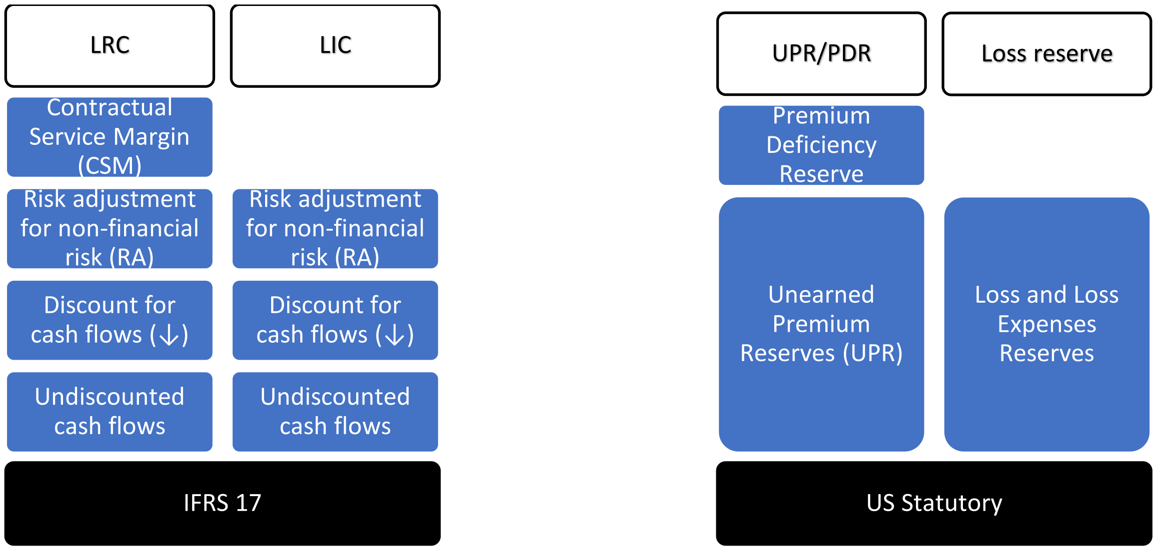
Prior to discounting, the LRC under the PAA when a group is onerous would be the same as for an onerous group under the GMM. For GMM, the CSM would be nil and when this occurs, the entity must recognize a loss which would increase the LRC.[33][34] There will be a reversal through the coverage period which will favorably impact the insurance service result (in the income statement). In the event that a group of contracts for which the LRC is determined using the PAA becomes onerous, the entity is required to compare the difference of the LRC_{PAA} (t) as defined above to the FCF underlying the LRC.[35] This calculation will need to recur with each subsequent evaluation as there could be a reversal of the group back to profitability, or a different level of loss.

At initial recognition, one incorporates the entirety of FCF and any cash already transferred between the parties to determine if, on a risk adjusted present value basis, the contract in question is onerous. If not, the anticipated profit within the LRC is the CSM (or expected profit under the PAA). As the contract ages, revenue will be recognized as the liabilities convert from covering future service to covering past service, with loss payments reducing the FCF. The figure below provides a comparison of IFRS 17 with US SAP as to the distribution of the liabilities:

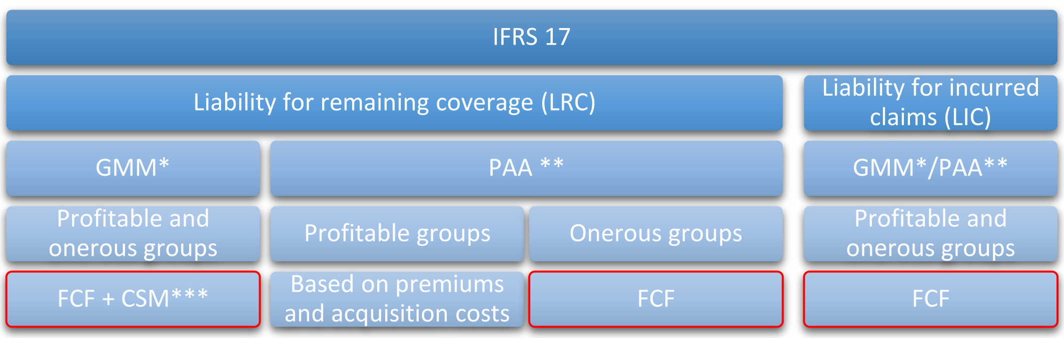
[33] IFRS 17 §58

[34] However, discount curve may differ.

[35] IFRS 17 §57



The figure below summarizes the components required when measuring LRC and LIC and shows when actuaries need to calculate FCFs:



* GMM = General Measurement Model
** PAA = Premium Allocation Approach
*** CSM = Contractual Service Margin

Under the PAA, although the FCF are not required when calculating the LRC for profitable contracts, a company may still want to project the FCF to determine if the contracts/groups become onerous.

Paragraph 41 of the Standard states that "*An entity shall recognize income and expenses for the following changes in the carrying amount of the* ***liability for remaining coverage****:*

(a) ***Insurance service revenue****—for the reduction in the LRC because of services provided in the period, measured applying paragraphs B120–B124;*

(b) ***Insurance service expenses****—for losses on groups of onerous contracts, and reversals of such losses (see paragraphs 47–52); and*

(c) ***Insurance finance income or expenses****—for the effect of the time value of money and the effect of financial risk as specified in paragraph 87."*

Paragraph 42 of the Standard states that "*An entity shall recognize income and expenses for the following changes in the carrying amount of the* ***liability for incurred claims****:*

*(a) I**nsurance service expenses**—for the increase in the liability because of claims and expenses incurred in the period, excluding any investment components;*
*(b) I**nsurance service expenses**—for any subsequent changes in fulfilment cash flows relating to incurred claims and incurred expenses; and*
*(c) I**nsurance finance income or expenses**—for the effect of the time value of money and the effect of financial risk as specified in paragraph 87."*

a) Insurance service result

Insurance service result, which will run through the statement of profit or loss represents the difference between the i**nsurance service revenue** and the **insurance service expenses**.

As discussed above, the i**nsurance service revenue** is calculated as the reduction of the LRC as services are provided. This is a reduction in the CSM under GMM, or as the release of the LRC under the PAA. The **insurance service expenses** are calculated as the changes in reserve estimates or reduction for the risk adjustment for non-financial risk.

Note that any investment components paid are excluded from the insurance service revenue and expenses.

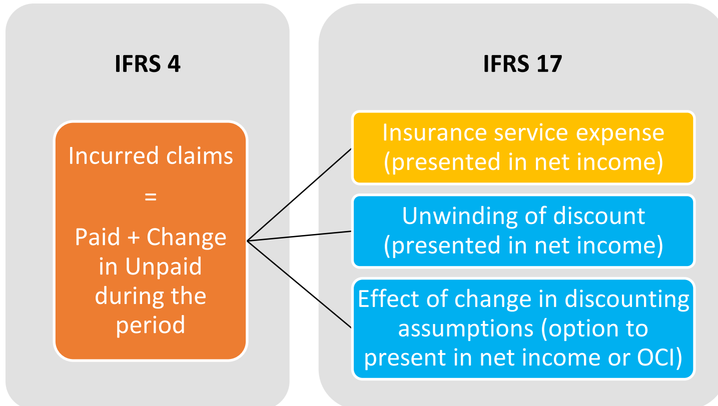
b) Insurance finance income or expenses

The Exposure Draft of the Proposed International Actuarial Note (IAN) 100 on Application of IFRS 17 Insurance Contracts states the following:

"Insurance finance income or expenses (refer paragraphs 87 – 92 and B128 – B136), for the effect of the time value of money and financial risk, includes:
- *Investment income earned on assets during the period, and*
- *The effect of discounting of the expected future cash flows. "*

c) Insurance Service Expenses and Insurance Finance Expenses from insurance contracts issued

Under IFRS 17, there is now a requirement to break down the incurred claims into **insurance service expense** (yellow box below) and **insurance finance expense** (sum of blue boxes below)**.**



The example below illustrates this concept. For this example, RA (risk adjustment) is excluded from the calculation.

Time (t)	*1*	*2*	*3*
Payments	*0*	*0*	*USD 1,000*

As at t=0, assuming a flat yield curve of 2%, the LIC is $1,000/(1.02^3) = $942.

As at t=1, assuming a flat yield curve of 2.5% and a new estimated payment cash flow of $*1,500, the LIC is* $1,500/(1.025^2) = $1,428. The following amounts need to be calculated:

- Unwinding: $1,000/(1.02^3)*0.02 = $19
- Effect of change in discounting rates: $1,000*(1/(1.025^2) - 1/(1.02^2)) = ($9)
- Insurance service expense: $1,500/(1.025^2) – $1,000/(1.025^2) = $476.

The sum of these three amounts is $486 and it corresponds to the change in the estimate of LIC ($1,428 – $942).

Section 4 - Disclosures in financial statements

Reconciliations

An entity shall disclose qualitative and quantitative information about the amounts recognized in its financial statements.

This will include detailed reconciliations of changes in insurance contract liabilities (LRC and LIC) from one reporting period to the next. Disclosure and reconciliations should be done separately for contracts issued and reinsurance contracts held[36], and to an appropriate level of aggregation (for example, by product line, by geographical area, or by reportable segment)[37].

Reconciliations will show the carrying amount at the beginning and at the end of the period, disaggregated into a total for portfolios of contracts that are assets and a total for portfolios of contracts that are liabilities, which equal the amounts presented in the statement of financial position.[38]

Reconciliation for amounts in the balance sheet[39]

An entity shall disclose reconciliations from the opening to the closing balances separately for each of:

- the LRC excluding the loss component;
- any loss component;
- the LIC.

In separate reconciliations for LRC (if GMM is used) and for LIC, an entity shall disclose the estimates of the present value of the future cash flows, the risk adjustment for non-financial risk and the CSM (LRC only).

Reconciliation for amounts in the income statement[40]

An entity shall disclose reconciliations separately for each of the following amounts related to services:

- insurance revenue
- insurance service expenses, showing separately the amounts

[36] IFRS 17 §82

[37] IFRS 17 §96

[38] IFRS 17 §99

[39] IFRS 17 §100-102

[40] IFRS 17 §103-106

- incurred claims (excluding investment components) and other incurred insurance service expenses;
- amortization of insurance acquisition cash flows;
- changes that relate to past service, i.e. changes in FCF relating to the liability for incurred claims;
- changes that relate to future service, i.e. losses on onerous groups of contracts and reversals of such losses; and
- investment components.

An entity shall also disclose separately each of the following amounts not related to services provided in the period, if applicable:

Cash flows in the period, including:

- premiums received for insurance contracts issued (or paid for reinsurance contracts held);
- insurance acquisition cash flows; and
- incurred claims paid and other insurance service expenses paid for insurance contracts issued (or recovered under reinsurance contracts held), excluding insurance acquisition cash flows;
- the effect of changes in the risk of non-performance by the issuer of reinsurance contracts held (i.e. provision for uncollectable reinsurance);
- insurance finance income or expenses; and
- any additional line items that may be necessary to understand the change in the net carrying amount of the insurance contracts.

If the measurement is done using GMM, additional reconciliations will need to be disclosed related to the LRC and its CSM.

Other Disclosures

If an entity selects the PAA to measure its insurance contract liabilities, the following should be disclosed:

- the criteria used to qualify for the PAA (i.e. coverage period not over a year or reasonable approximation of the LRC);
- whether it makes an adjustment for the time value of money and the effect of financial risk; and
- the method it has chosen to recognize insurance acquisition cash flows (i.e. deferred or recognized when incurred).[41]

[41] IFRS 17 §97

Other disclosures that will need to be added in the financial statements will be related to:

Significant judgments (IFRS 17 §117-120)

- **Inputs, assumptions and estimation techniques**
- **Additional disclosure for discounting**
  - Yield curve(s) used to discount cash flows
  - *Relationship between insurance finance income or expenses and the investment return on its assets*
- **Additional disclosure for RA**
  - Confidence level
  - Technique used to determine the confidence level if the entity uses a technique other than the confidence level technique
  - Whether or not discounting related to the RA is disaggregated between the insurance service result and insurance finance income or expenses

Nature and extent of the risks (IFRS 17 §121-132)

- **Type of risks** that arise from insurance contracts
  - <u>Insurance risks</u>
  - <u>Financial risks</u> (such as credit risk, liquidity risk and market risk)
- **Disclosure for all types of risks**
  - the exposures to risks and how they arise
  - the entity's objectives, policies and processes for managing the risks and the methods used to measure the risks
  - any changes in the two points above from the previous period
  - concentrations of risk (description of how the entity determines the concentrations, and a description of the shared characteristic that identifies each concentration)
  - sensitivity analysis (including the methods and assumptions used in preparing the sensitivity analysis)
  - Disclosure related to **insurance risk only**
    - claims development
  - Disclosure related to **credit risk only**
    - information about the credit quality of reinsurance contracts held
  - Disclosure related to **liquidity risk only**
    - separate maturity analyses for insurance contracts issued and reinsurance contracts held

Note that for nature and extent of risk disclosure requirements are really similar to what is required now, only at a more detailed level.

Conclusion

The purpose of the primer is to introduce the reader to important changes that will occur that will result from IFRS 17. In order to keep the paper amenable, many of the concepts are described on a broad basis. In order to fully grasp the extent of all the changes that will need to be considered, one would need to refer to the actual Standard and to work with experts who have studied the Standard over the past few years. Although challenging to implement, we believe the Standard will bring greater transparency and consistency to future financial disclosures provided by insurance companies.